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Chile's mining sector, considered the strategic linchpin of the country's economy, is undergoing a little-noticed but highly significant transformation through large-scale new private investment in extractive and related activities and a process of "creeping" privatization. Private investment in the mining sector is expected to surpass a whopping US$3 billion dollars in 1994 alone, and another US $2.17 billion is projected to flow in over the next three years, reflecting "a veritable boom" in the country's extractive industry, according to a recent Ministry of Mines report.

The report indicated that most of this new investment is directed at expanding copper production through the opening of new deposits and the modernization of existing mining facilities. Chile is currently the world's principal producer of copper, exporting a little more than 1.3 million metric tons of the metal in 1993 out of a total worldwide production for that year of 3.97 million MT, or approximately one-third of world output. With the projected expansion of the industry, exports are expected to surpass 3.4 million MT annually by the year 2000. Copper exports alone account for some 45% of the country's export earnings. The expansion of the mining industry is expected to help sustain Chile's current economic growth over the next several years. However, critics among them the country's labor unions and center-to-left political groups have warned that the expansion represents a perilous heightening of the country's traditional dependence on raw material exports in a precarious world market, and that a reduced role for the state in this strategic sector may diminish the social and economic benefits associated with increased production. "Creeping" privatization of the mining industry

Mining has been the linchpin of the Chilean economy ever since nitrates were discovered in the country's northern desert last century. With the depletion of nitrate deposits, copper came to dominate the national economy, accounting for more than half the country's exports by the 1960s and over one-fifth of the GDP. In 1971, socialist President Salvador Allende (1970-1973) nationalized the holdings of Anaconda and Kennecott, the two US-based companies that dominated the Chilean mining sector, and created the public Copper Corporation (Corporacion Nacional del Cobre de Chile, CODELCO) to manage the country's mineral production.

The Pinochet dictatorship (1973-1990) returned most properties expropriated during the Allende years to their former owners as part of its sweeping free-market restructuring of the economy. But it chose to make an exception regarding the mining sector.

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Although it opened the mining sector to new private investment, it retained state ownership over existing facilities and instead provided financial compensation to the expropriated US mining companies. Thus, in a highly paradoxical situation, foreign investment in the mining sector resumed in 1973, but the industry as a whole remained largely a state sector in an otherwise free-market economy and was seen as pivotal to the country's development. But the mining industry's seeming immunity to the free- market program began to erode under ex-president Patricio Aylwin's administration (1990-1994).

With the consolidation of neoliberal reform, the Aylwin government, especially in its final year in office, began to explore the prospects for the privatization of CODELCO holdings. Under Aylwin, there was an upsurge in state concessions of exploration and exploitation rights to private firms for huge mineral deposits around the country. But national laws prohibited any direct private sector investment in CODELCO-run facilities and thus prevented even partial privatization of CODELCO's current and planned operations. In the final months of its tenure, the Aylwin administration succeeded in having Congress approve a law that for the first time allowed CODELCO to solicit private bids for joint ventures with private capital in mineral production. At the time the law was passed in late 1993, CODELCO president Alejandro Noemi predicted that related projects undertaken henceforth by CODELCO would eventually be privatized.

Newly elected President Eduardo Frei promised upon taking office in February of this year that his administration would aggressively pursue the general privatization program begun by his predecessors, Aylwin and Pinochet. However, Frei has been adamant in affirming that the privatization program would not include CODELCO. He has reiterated this on several occasions since taking office, reflecting the highly controversial nature of privatization of the mining sector, including strong opposition among elements from within his own "Democratic Convergence" governing coalition. Nevertheless, it is clear that the government is pursuing a complex and contradictory policy of "creeping" privatization, and that this process, followed to its logical conclusion, will eventually undermine any commanding government control over the strategic mining sector.

According to this creeping-privatization scenario, the huge public CODELCO conglomerate, which currently generates approximately one-third of the state's export earnings, will not be privatized as such. Rather, a gradual reduction in the overall importance of the public sector in the country's mining industry will occur as a result of three processes. First is ongoing new private foreign and national investment in extractive activities. Of the US$5 billion in new investments in the mining industry projected for the next four years, the overwhelming majority is from private foreign investors. In the most important development in this regard, in May the US-based firm Cyprus Minerals purchased 51% of the shares for mining rights to the El Abra copper deposits for US$330 million. The company promised to invest US$299 million for start-up operations, and to raise an additional US$699 million in local financial markets. The new mine is expected to begin production in June 1997, and to generate some US$250 million in additional annual copper earnings. Once it is fully operational, the El Abra facility will be the world's largest copper mine.

Other recent new investments include an initial US$168 million invested this year by the US transnational Lac Mineral to open the Nevada gold mine in the north of the country, and an

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investment late last year of US$175 million to begin construction on a new open-pit copper mine in Mantoverde by the South American subsidiary of the huge South African-based transnational, Anglo America Corporation. Second, mining sites currently owned and operated by CODELCO are expected to gradually become exhausted in the remainder of the decade. Former CODELCO president Alejandro Noemi predicated late last year that over the next decade "CODELCO will be producing less copper because the ore grades in our mines are falling dramatically." Among those facilities that will eventually disappear are the El Teniente mine, the largest underground mine in the world, which is expected to exhaust all of its copper deposits early next century. And, production costs at the Chuqui mine are projected to rise steadily over the next several years as remaining deposits become more inaccessible and require greater labor costs and related expenditures for extraction, according to the mine's division manager, Renzo Gasparini.

As these sites are phased out and substituted by the opening up of new deposits to private commercial mining or by joint CODELDO-private undertakings, the percentage of total mining accounted for by CODELCO will gradually diminish. Indeed, by 1993 CODELCO's share in the country's mining sector had already accounted for only a little more than 40% of total output. Third and finally is the privatization of complementary enterprises that directly service the CODELCO conglomerate, such as mine-to-port railroads, mining industry warehouses and supply networks, and horizontal and vertical spin-off activities such as copper processing. In September, for instance, the incoming Frei administration finalized the privatization of the Pacific Railroad Company (Ferrocarriles del Pacifico de Chile, FEPASA), which, in addition to providing passenger transport, is also used to shuttle raw copper from mines to processing plants and ports around the country. Behind the push for free-market transformation of the mining sector are powerful Chilean and foreign business interests. Foreign firms have expressed special interest in the country's vast still untapped copper and gold reserves.

Not surprisingly, then, business organizations are steadily increasing their pressure on the government to privatize CODELCO holdings. In fact, a major scandal early this year over mismanagement of CODELCO's financial assets has galvanized the private sector and right-wing parties into action to lobby for CODELCO's total privatization. "CODELCO Earthquake" of early 1994 and Frei's ambiguous policy The mining sector was shaken in early 1994 by a scandal involving US$307 million in government losses in futures trading by CODELCO. The scandal, which was quickly dubbed the "CODELCO Earthquake," first broke in January, when the CODELCO president at the time, Alejandro Noemi, revealed that company officials had mismanaged speculative transactions in its futures sales on the London Metal Exchange. Futures trading are purchases of future production on international stock exchanges, on the basis of estimates of what world market prices will actually be at the time the product in this case copper is actually placed on the world market. In this highly speculative trading, a form of market gambling, a buyer may purchase in advance a quota of merchandise yet to be placed on the market and may at any time sell those quotas on the market for more or less than the original purchase price.

The CODELCO official directly responsible for the transactions, Juan Pablo Davila, admitted that he had purchased huge quantities of copper on the futures market on behalf of CODELCO and then turned around and resold these futures shares for less than the purchase price. Davila alleged that the loss was due to technical computer errors as he conducted the transaction with brokers and intermediaries in London through CODELCO's central computer terminals in Santiago. As

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the "CODELCO Earthquake" shook public opinion, Congress opened a formal investigation and the Ministry of Justice detained and began criminal proceedings against Davila and two other CODELCO executives. In August, the new CODELCO president, Juan Villarzu, announced that after seven months of investigations if was confirmed that Davila and his associates had engaged in criminally "defrauding the state."

Officials from the Frei administration acknowledged that criminal mismanagement indeed occurred, but argued that its right-wing opponents had blown the issue out of proportion to heighten pressure for the total privatization of the state mining sector. The country's principal right-wing party, the Independent Democratic Union (UDI), which is generally seen as representing the interests of Chile's powerful financial and industrial groups, did in fact release a sweeping proposal several weeks after the scandal erupted for the complete sale of CODELCO for US$13 billion, the estimated value of the conglomerate, according to UDI spokespeople.

The UDI proposal was immediately backed by the Confederation of Production and Commerce (Confederacion de la Produccion y el Comercio), which brings together the country's principal private sector associations. Then in late April, the National Association of Mineral Producers (Sociedad Nacional de Mineria, SONAMI) presented a detailed plan for the "gradual" privatization of CODELCO, starting with the breakup of CODELCO's five principal mining operations the Chuquicamata, La Exotica, El Salvador, El Teniente and Rio Blanco mines into autonomous corporations and the subsequent sale of each to private bidders.

Although the Frei government rejected the SONAMI proposal for the "phased" privatization of CODELCO, its own proposal for "modernizing" the state conglomerate, presented shortly after the new administration took office, is remarkably similar to SONAMI's proposal. The Frei plan, currently under debate in Congress, involves an internal reorganization of the conglomerate. In effect, CODELCO would devolve into a state holding company, which would be subdivided into autonomous branches overseeing each major mining operation. Management and decision-making would be decentralized, moving from the central board of directors to directors and managers in each of the subdivisions. Indeed, both the SONAMI and the government plan propose the same subdivision and decentralization, with the only difference being that the former argues that such a reorganization should be the first step in total privatization, while the government insists that existing CODELCO holdings should remain in state hands.

Moreover, the government plan contains two clauses that would facilitate partial and creeping privatization. First, it proposes that the CODELCO holdings other than mineral deposits may be privatized. These holdings include a thermoelectric plant in the north of the country that provides electrical power to the mines, warehouses that distribute mining equipment, and workshops that produce mining-related goods. Second, the draft explicitly encourages private investment in existing CODELCO facilities and new joint private sector-CODELCO undertakings.

Controversy over government mining policy

The government's twin strategy of dramatic expansion of copper production and creeping privatization of the mining industry has generated broad controversy. On the one hand, the Chilean right, organized principally into the UDI, has made privatization of CODELCO a major component

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of its own program, with the open support of Chilean private sector groups. On the other hand, left parties in Congress, including Socialist deputies who form part of the Frei's governing "Democratic Convergence" coalition, have opposed the government's plan to reorganize CODELCO, arguing that it constitutes an ominous first step toward outright privatization of the state mining sector. For their part, the opposition Communist Party and the powerful Federation of Copper Workers (Federacion de Trabajadores del Cobre, FTC), which brings together 25,000 state-sector mine workers, issued a joint statement following the introduction of the Frei government's reorganization proposal into Congress calling for a national "common front in defense of CODELCO."

The FTC and its backers among Socialists and Communists fear that the "modernization" and "creeping privatization" of CODELCO will result in massive layoffs and cuts in wages and benefits. Indeed, under the banner of modernization, CODELCO cut its work force by 7% in 1992, laying off 2,000 employees and sparking a spate of labor conflicts and work stoppages (see Chronicle, 5/13/93). Opposition to the privatization of CODELCO has made the country's leftist parties and mine workers strange bedfellows with a most unlikely ally the military, which currently receives a flat 10% of all CODELCO profits as part of the agreement it reached in 1990 with incoming civilian authorities for a transition from dictatorship to democracy.

Meanwhile, the strategy of maintaining export earnings and fueling economic growth through copper production has been severely criticized as a dangerous continuation of the country's extreme dependence on a single mineral. This danger became manifest when international copper prices experienced major fluctuations last year. In 1993, world market prices for copper plummeted, bottoming out at slightly below US$0.70 cents per pound, the lowest level since 1987. As a result, the Central Bank, which calculates that the country loses about US$22 million in annual income for every US$0.01 cent that the price per pound drops, reported a huge drop in export income in 1993. In turn, this loss of income was a major factor in last year's trade deficit of more than US$800 million..

By 1994, copper prices had once again rebounded, surpassing US$1.20 a pound on the Commodity Exchange of New York last month, the highest level in four years. Current high prices have triggered a boom. "Demand is so strong that warehouse operators cannot ship copper to customers as fast as they would like, forcing copper consumers to wait weeks for deliveries," said Richard Hirsch, an official of one brokerage house in New York. Ironically, the 1993 drop in copper prices was attributed to the increase in world output that took place in 1992, which drove global copper stocks up and created a glut that pushed prices down. Therefore, critics argue, the planned dramatic expansion by Chile of its copper production is a self- defeating strategy, since major new output will only push down prices again, which in turn will greatly diminish the benefits of increased production.

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